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ABSTRACT

Intended to provide a basic understanding of the history and complexity of a relatively new foreign currency measure, this paper briefly describes the history leading to the formation of the European Economic Community (EEC), its objectives, its governance structure, and its development of the European Currency Unit (ECU) as a means of stabilizing Europe's monetary system and strengthening the ties of the EEC's 11 member nations. Described as an intangible, cashless currency much like automated bank transfers, the value of an ECU is based on an average of all participating currencies. Should the ECU become independent of the fluctuating U.S. dollar, it could become a major currency of both account and settlement, creating a regional currenty in Western Europe. The recent decisions of Spain and Portugal to join the EEC (often referred to as the Common Market) have enlarged the community market, but the implications of the ECU for Americans in the financial and business community remain to be determined.

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THE EUROPEAN CURRENCY UNIT:
AN ECONOMICAL, FINANCIAL, AND POLITICAL CURRENCY

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INTRODUCTION

American business interests are local, national, continental, and worldwide in scope. Business operations often require transactions that occur in currency other than the United States Dollar. The American Institute of Certified Public Accountants, the Internal Revenue Service, and the Security and Exchange Commission have established guidelines for converting foreign currency transactions to dollar equivalents in certain circumstances. SFAS 33, SFAS 52, and SFAS 70, issued by the American Institute of Certified Public Accountants, require foreign currency translations for financial reporting purposes. SFAS 52 gives the objectives of foreign currency translation as:

1. to provide information disclosing the effects of rate changes on enterprise cash flows and equity; and

2. to provide information in consolidated statements relative to the financial results of individual consolidated entities as measured by the functional currency of each reporting entity.

Americans in the financial and business community need to have a basic understanding of the history and complexity of a relatively new foreign currency measure called the European Currency Unit (ECU), the official currency of the European Economic Community, (EEC).

HISTORY LEADING TO FORMATION OF THE EEC

In order to gain an understanding of the EEC, it is necessary to review the steps leading up to the formation of the EEC. The end of World War II found the continent in ruins, impoverished, and deeply divided. It was time for European countries to work together to improve their economical, financial, and political relationships among themselves and other countries.

With Russia occupying portions of Europe and virtually on the doorstep of Western Europe and Great Britain, Winston Churchill called for Europe not only to unite financially, but also politically and militarily. In 1946 he stated, "We must build a kind of United States of Europe." The idea of a community of European countries working together to solve their common problems received some measure of support, but no action to implement the suggestion was taken. Charles de Gaulle opposed

any joint organization of France with Great Britain.

Six Western European countries-- France, the Federal Republic of Germany, Italy, Belgium, the Netherlands, and the Grand Duchy of Luxembourg--took action on the economic front. In an effort to protect coal and steel workers in their countries they formed the European Coal and Steel Community in 1950. This successful community was the forerunner for a more complex union.

The six countries of the European Coal and Steel Community chose to extend their cooperative efforts in 1957 by forming The European Economic Community (EEC), commonly referrred to as the Common Market. In addition, they integrated the Coal and Steel Community into the EEC. The EEC has a separate identity from its individual member states. The policies of this new community cover a full range of cooperative effort, beginning with economical cooperation and extending to educational, political, financial, and social integration for all EEC countries.

The EEC has continued to expand its influence in Europe. By 1985 the Community consisted of the original six countries plus three others, Great Britain, Denmark, and Greece. On January 1, 1986 the total member countries will increase to eleven when Spain and Portugal join the Community.

THE EEC TODAY

The major objective of the EEC is to provide for peace and prosperity in Europe through an integration of the economic policies of its member nations. Over time, they have developed many common positions on a wide range of social and trade policies. For example, they eliminated tariffs and quotas for goods traded between EEC members and set common tariffs and quotas for goods shipped from outside the EEC.

How does the EEC meet its objectives? It looks to its five governmental institutions to set and enforce policy, and it raises revenues to fund those institutions. Revenues are raised from two sources, all duties on products imported from outside the Community and a percentage of the value added tax of each member county. In 1985 these two sources of funds are used to support a budget of 27.9 billion ECU's which is equivalent to $20 billion United States dollars.

The five governmental units that guide the Community are the European Commission, The Council of Ministers, the European Council, the European Court of Justice and the European Parliament. Careful planning went into the development of these five governmental bodies. Keep in mind when thinking about the EEC that the Community is composed of individual countries, some of whom ruled large empires and had amassed great power and wealth. It is sometimes difficult for these countries to function as a part of a larger cooperative Community.

THE EUROPEAN ECONOMIC COMMUNITY- GOVERNMENT

Authority		Institution		Function
Appointed by Member Governments	----->	EUROPEAN COMMISSION	------>	Carries on Daily Operations
Member States Representative	----->	COUNCIL OF MINISTERS	------>	Decision Makers
Heads of Member States	----->	EUROPEAN COUNCIL	------>	Real Decision Makers with Veto power
General Elections	----->	EUROPEAN PARLIAMENT	------>	Forum of the European Community
Jointly Appointed by Member States	----->	EUROPEAN COURT OF JUSTICE	------>	Legal Rulings on EEC & ECSC Treaties

All EEC countries must conduct democratic elections in order to belong to the Community. Members of the European Parliament are elected during general elections held in their own country. When they meet they provide a forum for discussion of issues in a free and open manner. However, they have little power in the setting of EEC policy.

Each member state appoints a representative to sit in the Council of Ministers. These are the real decision makers on most issues. But, the discussions conducted in the European Parliament may affect the decisions made by the Council of Ministers.

All decisions must meet the approval of the European Council. The council consists of the head of each member state. One of the councils major weaknesses or possibly one of it's major strengths, depending on your point of view, is the veto power

that can be exercised by each head of state. Any issue can be blocked by one leader.

Once a decision has been made by the Council of Ministers or the European Council it's implementation is turned over to the European Commission. The Commissioners are appointed by each member Government and are responsible for the day to day operations of the EEC. The commission is located in Brussels, Belgium and pays the salaries of over 19,000 employees, better known as Eurocrats.

An extremely important and powerful body is the European Court of Justice. Justices are appointed jointly by member states. They make binding legal rulings relating to the treaties that set up the EEC and the European Coal and Steel Community (ECSC).

THE EUROPEAN CURRENCY UNIT

One of the problems facing the EEC is the wide fluctuations in the currencies of some member states which resulted from both internal and external economic forces. The combined affect of the oil crisis, double digit inflation, the U.S. going off the gold standard, and high U.S. interest rates increased the instability of many of the European currencies. Each member state was setting its own monetary alignment policy, with the result that some currencies were fluctuating wildly.

Monetary stability became an important goal for the EEC. In order to achieve that goal they established in 1979 a European Monetary System which uses the Economic Currency Unit (ECU) as the cornerstone for this entirely new financial system. Since then, the use of this intangible monetary currency has grown rapidly. For example, all payments by the ECC such as salaries, loans, and regular budget items are made in ECU's. Also, all intra-community duties and farm prices are expressed in ECU's.

How is the value of an ECU determined? It is intangible, you cannot see it or feel it, no bills have been printed or coins minted. It is a cashless currency, much like automatic bank transfers. It's value at any one time is based on the average of all participating Community currencies. If the value of the German mark goes up while the value of the Italian lire goes down the ECU will be affected by both events, neither gaining as much value as the mark or losing as much value as the lire. Rates can vary daily based on the fluctuations of the ten individual currencies which combine to determine the value of the ECU. Those daily rates are published in the official journal of the European communities.

Although the computation of the value of the ECU is based on an average of all participating currencies, the amount of each national currency remains constant for five years. For example from January 1, 1979 until August 31, 1984 the value was composed

of the amount of 109 Italian lire. The equivalent of the ECU in any currency is equal to the sum of the equivalents of these amounts in that currency. Per council regulation, the value of the ECU was composed of the amounts of these national currencies as follows:

January 1, 1979 -- August 31, 1984

0.828	German mark	3.66	Belgium francs
0.0885	pound sterling	0.14	Luxembourg franc
1.15	French francs	0.217	Danish krone
109.	Italian lire	0.00759	Irish pound
0.286	Dutch guilder		

September 1, 1984 -- ??

0.719	German mark	3.71	Belgium francs
0.0878	pound sterling	0.14	Luxembourg franc
1.31	French francs	0.219	Danish krone
140.	Italian lire	0.00871	Irish pound
0.256	Dutch guilder	1.15	Greek drachmas

The ECU is considered a basket-type currency--a basket designed to expand to include future member countries currency. The currencies of Spain and Portugal will be included in the future. In 1985 the basket consisted of 0.719 German mark, 0.0878 pound sterling, 1.31 French francs, and the seven other currency amounts as listed above under the September 1, 1984 figures.

CONCLUSION

The American Institute of Certified Public Accountants, The Internal Revenue Service, and the Security and Exchange Commission require foreign currency translation in certain circumstances. A new emerging foreign currency, the ECU, may affect Americans in the financial and business community. The ECU is the official currency of the EEC.

A possible emerging giant which may have a pronounced effect is the EEC. The goals of integrating the member countries as a whole has not yet been achieved. However, the creation of a common market where goods and people would circulate freely has had some level of success. It is impossible to predict how successful the EEC will be in promoting the ECU within the Community or outside the Community. However, the ECU is seen as strengthening the ties of the member nations. If a more homogeneous Europe is the result, the ECU may become independent of the fluctuating United States dollar and may become a major currency of both account and settlement, creating a regional currency in Western Europe.

A source of pride emulates from the decision of both Spain and Portugal to join the EEC, enlarging the community market.

Unfortunately, this has possible negative ramifications for Florida and the United States, resulting from the fact that both Haiti and Cuba may lose their major export markets over the next five years to the two new common market countries. Already the U.S. citrus industry has been hurt by the Community trade bargaining barriers. In addition, Europe has been dumping its agricultural glut on the world market at unreasonably low prices affecting U.S. trade relations.

What impact will the ECU have on financial statements published in the United States? Currently there is no definite answer. However, the monetary currency of this new-type economic association, the EEC has to be taken into consideration by other countries of the world.

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